

RATING REPORT

Matco Foods Limited (MFL)

REPORT DATE:

January 6, 2021

RATING ANALYSTS:

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RATING DETAILS

Rating Category	Latest Rating		Previous Rating	
	Long-term	Short-term	Long-term	Short-term
Entity	A-	A-2	A-	A-2
Rating Outlook	Stable		Positive	
Rating Date	January 6, 2020		December 10, 2019	

COMPANY INFORMATION

Incorporated in April 1990	External auditors: Grant Thornton Anjum Rahman Co. Chartered Accountants
Listed Public Limited Company	Chairman of the Board: Mr. Jawed Ali Ghori
Key Shareholders (with stake 5% or more):	Chief Executive Officer: Mr. Khalid Sarfaraz Ghori
Ghori Group – 60.6%	
International Finance Corporation – 15.0%	
General Public (Local)- 15.3%	

APPLICABLE METHODOLOGY(IES)

VIS Entity Rating Criteria: Industrial Corporates (May 2016)

<http://vis.com.pk/docs/Corporate-Methodology-201605.pdf>

Matco Foods Limited (MFL)

OVERVIEW OF THE INSTITUTION

RATING RATIONALE

Initially, Matco Foods Limited (MFL) was incorporated under the name of Mohammed Ali Trading Company (Matco) in 1964. However, the company was subsequently converted into a private limited company in 1990 as Matco Rice Processing (Private) Limited. With change in business strategy, the company was renamed to Matco Foods (Private) Limited. In 2017, the company was converted into a public limited company.

Profile of Chairman

Mr. Jawed Ali Ghorri has over 40 years of experience pertaining to rice exports business, rice processing and development of rice industries. He also serves as Chairman to the Board of Directors at MFL.

Profile of CEO

With experience of over 30 years in the purchase and processing of rice, Mr. Khalid Ghorri utilizes his vast experience in assessing the qualities of agri-products and oversees the procurement and production process. His insights into crop survey and harvest are aimed to help farmers and Matco to achieve procurement targets. Mr. Khalid Ghorri graduated from University of Karachi in 1981 and pursued an article ship from ICAP (Institute of Chartered Accountants of Pakistan) Karachi between 1981 and 1984.

Matco Foods Limited ('MFL' or 'the Company') is in the business of processing and export of rice, rice glucose, rice protein and trade of biscuits, pink salt, bran oil, masala and kheer. The company operates rice processing and milling plants situated in Sadhoke, Punjab and Karachi, Sindh.

Industry and Business Risk

- In FY20, Pakistan's rice export revenue increased to an all-time high of USD2.175bn registering, showcasing a YoY increase of USD 106mn.
- Pakistan's overall rice exports, in volumetric terms, increased marginally by 1.1%, mainly as the pandemic-induced slowdown took a toll on global trade volumes.
- Pakistani Basmati rice exports registered 34.97% growth in terms of volumes and 24.63% growth, in terms of value, with EEU being the leading importer.
- A potential area for future growth is the Chinese market, wherein access is limited on account of domestic quota system in place in China. A government level negotiation could ease the way for increasing Pakistani rice exports to China.
- Newly added export market of Saudi Arabia is expected to grow as KSA is set to follow the footsteps of EU for implementing pesticide residue regulations. These will help Pakistani exports, which are compliant with pesticide residue regulations.
- Exports to Qatari market are also expected to gradually pick up pace.
- India has claimed exclusivity on the brand name of Basmati rice in the EU. In response, GoP has filed an application against the motion, in coordination with Rice Exports Association of Pakistan (REAP). This posts operational risk on Pakistan's Basmati Rice exports.
- So far, in FY21, the rice exports of Jul-Oct'20 declined by 29% and 21% in terms of value and volume respectively. In view of aforementioned developments, we expect industry growth of FY21 to come negative in terms of value as PKR is expected to stay stable in near term against USD.

Table 1: Pakistan Rice Exports (PBS)

Variety	Pakistan (PBS)					
	Jul-19 to Jun-20		Jul-18 to Jun-19		% Change	
	Qty (MT)	Value "000" \$	Qty (MT)	Value "000" \$	Qty MT	Value "000" \$
Rice (Basmati)	890,207	790,792	659,571	634,532	34.97%	24.63%
Rice (Other)	3,275,923	1,384,701	3,460,566	1,435,086	-5.34%	-3.51%
Total Sales	4,166,130	2,175,493	4,120,137	2,069,618	1.12%	5.12%

Operational Update

- In the segment where MFL operates, specifically Hotels, Restaurants and Catering (HORECA), has been badly affected by the pandemic-related lockdown. Tourism related sales and demand has been affected, particularly on account of curtailment of Haj season & and stoppage of Umrah. However, there has been a surge in demand for home-based consumption, and retail market has seen a jump in demand as a result of stockpiling.
- The management at MFL was proactive in adopting to the operational challenges arising from the pandemic. Safety measures were instituted across the company and 'Work from Home' was adopted, wherever possible.
- The capacity utilization of the rice processing segment was recorded higher in 2020 at 81% (2019: 61%). Capacity utilization of the rice glucose segment was lower at 31% (FY19: 41%). The drop can be attributed to new capacity coming online in FY20.

Topline has posted strong growth, albeit gross & net margins were compromised

- In FY20, MFL reported revenue of Rs. 11.3b, 44% higher than FY19 (Rs. 7.9b). Exports % in overall sales inched up to 77% (FY19: 73%). About two-thirds of the topline growth emanated from volumetric growth while about a third emanated from pricing increase, mainly on account of the rupee depreciation.
- In rice segment, Basmati exports sales posted strong volumetric growth of 30% YoY. Irri exports significantly grew to 6,698 Tons from 2,284 Tons. Besides this, given induction of new local market for rice glucose segment, the segment posted volumetric growth of 66%.
- MFLs gross margin has come under pressure in FY20, a trend which continued in Q1'FY21 (Q1'FY21: 5.9%; FY20: 9.0%; FY19: 11.6%). As per management, the drop in margins is mainly attributable to a sizable brown rice shipment, wherein the margins realized were lower than expected; this was a result of higher raw material price and volatility in the FX market. Margins are expected to remain under pressure in Q2'FY21 and post recovery in the subsequent quarters.
- As an exporter, the company is entitled to debt at concessionary rate under SBP's export refinance policy. Accordingly, despite significantly higher interest rates during FY20, the cost of debt (calculated on a two-point average) only increased from 6.1% to 6.8%. Cost of debt for Q1'FY21 was notably lower at 4.5%.
- Other income and exchange gain were much lower at Rs. 71m vis-à-vis Rs. 260m in the preceding year.
- Given the pressure on gross margin, higher finance cost and lower other income & exchange gain, the company's net margin contracted to 1.3% (FY19: 5.3%). Moreover, sizable exchange loss and unusual losses on FE-25 loan agreement due to fluctuation in USD prices made the bottom line negative in Q1'FY21 (Net Margin: -3%). In absolute terms, MFL incurred a net loss of Rs. 83mn during 1QFY21 (Net Income 1QFY20: 57.4mn).

Table 2: Sales Breakup

	FY19			FY20		
	Qty (MT)	Rs./MT	Value (Rs. Mn)	Qty (MT)	Rs./Unit	Value (Rs. Mn)
Rice						
Basmati (Exports)	40,135	135,966	5,457	52,051	152,965	7,962
Basmati (Local)	6,482	131,287	851	5,352	144,806	775
Irri (Export)	2,284	72,680	166	5,698	100,913	575
Total	48,901	132,390	6,474	63,101	147,573	9,312
Rice Glucose/Protein						
Rice Protein	1,216	98,684	120	1,252	128,594	161
Rice Glucose (Export)	810	133,333	108	1,246	146,870	183
Rice Glucose (Local)	4,924	58,692	289	8,161	63,350	517
Total	6,950	74,388	517	10,659	80,777	861
Other Items						
Maltodextrin (Local)	-	-	-	142	98,592	14
Export (NPD)	N/A	N/A	9.1	N/A	N/A	17.2
Local (NPD)	N/A	N/A	20.7	N/A	N/A	44
By- Product	31,213	33,223	1,037	39,180	33,563	1,315
Total	31,213	34,179	1,066	39,322	35,351	1,390
Total Sales	87,064	92,551	8,057	113,082	102,254	11,563

Cashflow coverage indicators have come under pressure, albeit this is likely to be a short-term trend

	FY18	FY19	FY20	Q1'FY21
Operating Cycle (Days)	343	304	243	235
- Debtor Days	37	44	43	34
- Inventory Days	320	273	236	224
- Payable Days	14	13	36	22
FFO	390	350	382	22
FFO - Debt	8.8%	7.7%	6.7%	1.6%*
FFO – Long Term Debt	105%	85%	64%	13%*
DSCR	1.84x	1.71x	1.61x	1.02x*
*Annualized				

- The company’s debt is largely (88%) short-term and the requirement for the same mainly arises from an elongated inventory cycle. Nevertheless, improvement has been noted in the same over the years, as also depicted in the table above. The short-term debt is also adequately covered by stock of inventory and trade debts, with the same constituting 1.5x of the short term borrowings as of Sep’20.
- As depicted in the table above, FFO has contracted in the most recent period, as a result of which cash flow coverage indicators have been impacted. Nevertheless, this is expected to be a short term trend. Accordingly, a rebound in FFO is projected; nevertheless, given our expectation of stiff pressure on margins, the FFO is unlikely to recover to fully, atleast in the ongoing fiscal year.

Capitalization

	FY18	FY19	FY20	Q1'FY21
Equity	3,582	4,062	4,146	4,070
Gearing	1.24x	1.12x	1.38x	1.39x
Leverage	1.37x	1.25x	1.70x	1.62x

- Equity base (excluding surplus on revaluation of assets) witnessed a 2% increase in FY20 as dividend payout increased to 36% as % of earnings from 21% in FY19. In 1Q'FY21, equity declined by 2% because of net loss incurred during the period.
- Gearing & leverage indicators posted marginal increase, which is mainly attributable to the business volume driven growth in debt and limited growth in equity amidst depressed profitability. Going forward, capitalization metrics warrant improvement, as they stand on the higher side.

Corporate Governance

- Board composition is line with best practices.
- Board of Directors comprises 9 members including 4 independent directors, 1 non-executive director, 2 executive directors, CEO and the Chairman.
- The Board also consists of 2 female directors (Non-executive and Independent director) which further reaffirms sound governance framework.

Matco Foods Limited
Appendix I
FINANCIAL SUMMARY
(amounts in PKR millions)

BALANCE SHEET	30-Jun-19	30-Jun-20	30-Sep-20	
Non-Current Assets	2,744.6	5,166.1	5,123.3	
Stock-in-Trade	5,204.9	6,642.5	6,447.8	
Trade Debts	941.1	1,334.5	1,029.5	
Short Term Loans & Advances	355.3	118.6	215.9	
Cash & Bank Balances	78.4	298.3	184.2	
Total Assets	9,574.9	13,836.3	13,267.5	
Trade and Other Payables	248.1	1,015.2	628.8	
Short Term Borrowings	4,139.2	5,115.9	4,951.0	
Long Term Debt (Inc Current Maturity)	409.8	596.6	695.6	
Total Interest Bearing Debt	4,549.0	5,712.5	5,646.6	
Total Liabilities	5,068.0	7,068.2	6,582.3	
Paid Up Capital	1,224.0	1,224.0	1,224.0	
Total Equity (Exc Revaluation Surplus)	4,061.8	4,145.9	4,069.7	
INCOME STATEMENT	FY19	FY20	Q1'FY20	Q1'FY21
Net Sales	7,863.1	11,290.0	2,107.2	2,795.6
Cost of Sales	6,948.5	10,274.0	1,851.7	2,630.3
Gross Profit	914.0	1,016.0	255.5	165.2
Distribution Expenses	167.1	207.0	44.1	50.6
Administrative Expenses	240.3	271.4	62.5	65.5
Other Income	106.7	56.5	6.6	6.6
Finance Cost	275.5	350.3	67.5	63.2
Profit / (Loss) Before Tax	460.5	238.5	75.9	(61.9)
Taxation	46.7	86.6	18.5	20.9
Profit After Tax	413.8	151.9	57.4	(82.8)
RATIO ANALYSIS	30-Jun-19	30-Jun-20	30-Jun-20	
Gross Margin (%)	11.6%	9.00%	5.91%	
PBT Margin (%)	5.86%	2.11%	-2.21%	
Net Margin (%)	5.26%	1.35%	-2.96%	
Current Ratio (x)	1.48	1.37	1.40	
Gearing (x)	1.12	1.38	1.39	
Debt Leverage (x)	1.25	1.70	1.62	
FFO	349.8	381.7	21.9	
FFO to Total Debt (%)	7.7%	6.7%	1.6%*	
Debt Servicing Coverage Ratio (x)	1.71	1.61	1.02*	
ROAA (%)	4.44%	1.3%	-2.44%*	
ROAE (%)	10.83%	3.70%	-8.06%*	

*Annualized

ISSUE/ISSUER RATING SCALE & DEFINITIONS

Appendix II

RATING SCALE & DEFINITIONS: ISSUES / ISSUERSMedium to Long-Term**AAA**

Highest credit quality; the risk factors are negligible, being only slightly more than for risk-free Government of Pakistan's debt.

AA+, AA, AA-

High credit quality; Protection factors are strong. Risk is modest but may vary slightly from time to time because of economic conditions.

A+, A, A-

Good credit quality; Protection factors are adequate. Risk factors may vary with possible changes in the economy.

BBB+, BBB, BBB-

Adequate credit quality; Protection factors are reasonable and sufficient. Risk factors are considered variable if changes occur in the economy.

BB+, BB, BB-

Obligations deemed likely to be met. Protection factors are capable of weakening if changes occur in the economy. Overall quality may move up or down frequently within this category.

B+, B, B-

Obligations deemed less likely to be met. Protection factors are capable of fluctuating widely if changes occur in the economy. Overall quality may move up or down frequently within this category or into higher or lower rating grade.

CCC

Considerable uncertainty exists towards meeting the obligations. Protection factors are scarce and risk may be substantial.

CC

A high default risk

C

A very high default risk

D

Defaulted obligations

Short-Term**A-1+**

Highest certainty of timely payment; Short-term liquidity, including internal operating factors and / or access to alternative sources of funds, is outstanding and safety is just below risk free Government of Pakistan's short-term obligations.

A-1

High certainty of timely payment; Liquidity factors are excellent and supported by good fundamental protection factors. Risk factors are minor.

A-2

Good certainty of timely payment. Liquidity factors and company fundamentals are sound. Access to capital markets is good. Risk factors are small.

A-3

Satisfactory liquidity and other protection factors qualify entities / issues as to investment grade. Risk factors are larger and subject to more variation. Nevertheless, timely payment is expected.

B

Speculative investment characteristics; Liquidity may not be sufficient to ensure timely payment of obligations.

C

Capacity for timely payment of obligations is doubtful.

Rating Watch: VIS places entities and issues on 'Rating Watch' when it deems that there are conditions present that necessitate re-evaluation of the assigned rating(s). Refer to our 'Criteria for Rating Watch' for details. www.vis.com.pk/images/criteria_watch.pdf

Rating Outlooks: The three outlooks 'Positive', 'Stable' and 'Negative' qualify the potential direction of the assigned rating(s). An outlook is not necessarily a precursor of a rating change. Refer to our 'Criteria for Rating Outlook' for details. www.vis.com.pk/images/criteria_outlook.pdf

(SO) Rating: A suffix (SO) is added to the ratings of 'structured' securities where the servicing of debt and related obligations is backed by some sort of financial assets and / or credit support from a third party to the transaction. The suffix (SO), abbreviated for 'structured obligation', denotes that the rating has been achieved on grounds of the structure backing the transaction that enhanced the credit quality of the securities and not on the basis of the credit quality of the issuing entity alone.

(blr) Rating: A suffix (blr) is added to the ratings of a particular banking facility obtained by the borrower from a financial institution. The suffix (blr), abbreviated for 'bank loan rating' denotes that the rating is based on the credit quality of the entity and security structure of the facility.

'p' Rating: A 'p' rating is assigned to entities, where the management has not requested a rating, however, agrees to provide informational support. A 'p' rating is shown with a 'p' subscript and is publicly disclosed. It is not modified by a plus (+) or a minus (-) sign which indicates relative standing within a rating category. Outlook is not assigned to these ratings. Refer to our 'Policy for Private Ratings' for details. www.vis.com.pk/images/policy_ratings.pdf

'SD' Rating: An 'SD' rating is assigned when VIS believes that the ratee has selectively defaulted on a specific issue or obligation but it will continue to meet its payment obligations on other issues or obligations in a timely manner.

REGULATORY DISCLOSURES		Appendix III			
Name of Rated Entity	Matco Foods Limited				
Sector	Food				
Type of Relationship	Solicited				
Purpose of Rating	Entity Rating				
Rating History	Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
	RATING TYPE: ENTITY				
	6-Jan-20	A-	A-2	Stable	Maintained
	10-Dec-19	A-	A-2	Positive	Maintained
	15-Nov-18	A-	A-2	Stable	Reaffirmed
	01-Jan-18	A-	A-2	Stable	Reaffirmed
	4-Apr-17	A-	A-2	Stable	Reaffirmed
	28-Dec-15	A-	A-2	Stable	Reaffirmed
	29-Dec-14	A-	A-2	Stable	Reaffirmed
	15-Jun-12	A-	A-2	Stable	Reaffirmed
	12-Jun-12	A-	A-2	Stable	Upgrade
27-May-11	BBB+	A-3	Stable	Upgrade	
Instrument Structure	N/A				
Statement by the Rating Team	VIS, the analysts involved in the rating process and members of its rating committee do not have any conflict of interest relating to the credit rating(s) mentioned herein. This rating is an opinion on credit quality only and is not a recommendation to buy or sell any securities.				
Probability of Default	VIS' ratings opinions express ordinal ranking of risk, from strongest to weakest, within a universe of credit risk. Ratings are not intended as guarantees of credit quality or as exact measures of the probability that a particular issuer or particular debt issue will default.				
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Due Diligence Meetings Conducted	Name	Designation	Date		
	Mr. Muhammad Farooqui	CFO	December 22, 2020		
	Mr. Faizan Ali Ghorji, CFA	Executive Director			